OFFICE OF INSPECTOR GENERAL
for the Millennium Challenge Corporation

AUDIT OF THE MILLENNIUM CHALLENGE CORPORATION'S FUNDING OF ACTIVITIES IN TANZANIA

AUDIT REPORT NO. M-000-11-003-P
March 30, 2011

WASHINGTON, DC

Office of Inspector General
for the Millennium Challenge Corporation

March 30, 2011

Mr. Daniel Yohannes
Chief Executive Officer
Millennium Challenge Corporation
875 Fifteenth Street, NW
Washington, DC 20005

Dear Mr. Yohannes:

This letter transmits the Office of Inspector General's report on the Audit of the Millennium Challenge Corporation's Funding of Activities in Tanzania. In finalizing the report, we considered your written comments on our draft report and included those comments in their entirety in appendix II of this report.

The report contains three recommendations to strengthen the Millennium Challenge Corporation's policies and procedures. We consider that a management decision has not been reached on Recommendation 1 because the Millennium Challenge Corporation did not agree with our recommendation. We consider that management decisions have been reached on Recommendations 2 and 3. Final action will not be reached on Recommendations 2 and 3 until the Millennium Challenge Corporation provides additional documentation.

I appreciate the cooperation and courtesy extended to my staff during this audit.

Sincerely,

Alvin A. Brown /s/
Assistant Inspector General
Millennium Challenge Corporation

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SUMMARY OF RESULTS

In February 2008, the Millennium Challenge Corporation (MCC) signed a 5-year, $698 million compact with Tanzania aimed at reducing poverty and stimulating economic growth through investments in the transportation, energy, and water sectors. The compact included $373 million primarily for road improvements, $206 million to improve the reliability and quality of electric power and extend electricity service to unserved communities, and $66 million to increase the availability of potable water, plus funding for administration of the compact. The compact entered into force in September 2008 and will conclude in September 2013. Execution of the compact takes place through the Millennium Challenge Account-Tanzania (MCA-T), the host government entity charged with implementing the terms of compact. As of June 2010, MCA-T had committed $281 million for the Tanzania compact.

The objective of the audit was to determine whether MCC has identified and mitigated the major risks related to the Tanzania compact in order to ensure that select project activities are completed on schedule, within budget, and before the compact ends.

The audit found that MCC did not identify and completely mitigate the major risks related to the Tanzania compact, and as a result, the compact activities will not be completed within budget and may not be completed on schedule. During the due diligence process prior to compact signing, when MCC analyzed the viability of the proposed projects, MCC did not identify several significant risks. This led to substantial changes during implementation, including the cancellation of a major energy project (page 3). For other risks MCC identified during due diligence or implementation through December 2010, not all of MCC's mitigation efforts were sufficient. In particular, funding for a budget shortfall is not guaranteed (page 4), and MCC's approach to ensuring worker safety and livelihood needs improvement (page 5). Furthermore, delays could occur if MCC's other mitigation efforts fail (page 7).

When MCC signed the compact in 2008, critical information surrounding several major projects was lacking, which led to problems during implementation. For example, the compact included a $53 million hydropower plant construction project, but MCC was unaware of environmental risks that had been identified at the site in 2005. These risks ultimately led to the project's cancellation, disappointing residents in the region who have very limited electrical service. As a result of inadequate due diligence, MCC made substantial changes to projects during implementation, reducing the level of service agreed to in the compact (page 3).

Despite cancellation of the $53 million hydropower plant, MCC officials anticipate a budget shortfall of up to $134 million, primarily in the transport sector, which they attribute to rising construction costs. MCC will rely upon the Government of Tanzania to fund the shortage, but the Government may not be able to provide the funds in a timely manner (page 4).

Furthermore, MCC's policies do not adequately address workers' safety and livelihood. The audit found that the contractor for a road construction project did not provide proper induction safety training, adequate personal protective equipment, or water to workers on the site. The contractor also did not properly compensate some workers for overtime. The audit also found that the Health and Safety Management Plans prepared by two different road construction contractors varied significantly in specificity and practicality. Without consistent safety standards and proper monitoring of contractor compliance with the safety plans, MCC is risking worker safety and jeopardizing project completion (page 5).

Finally, the transport and energy projects face considerable risks that could delay their completion if MCC's mitigation efforts fail. For example, contractors have encountered delays in the tax exemption process when receiving shipments from the port, which limits their access to imported equipment and may contribute to project delays. MCC has recognized the significance of these risks and has taken steps to mitigate them (page 7).

The report recommends that MCC:

1. Amend its compact development policy to identify the requisite studies that will be completed prior to compact signing (page 4).

2. Monitor the Government of Tanzania's progress toward meeting the milestones that MCC has outlined for funding the budget shortfall, document decisions made during this process, and report to OIG regarding the Government's efforts (page 4).

3. Strengthen MCC's occupational health and safety policy by (a) adopting international best practices, (b) providing guidance to MCAs on implementing the policy, (c) developing standards for contractors' Health and Safety Management Plans, and (d) establishing worker safety and livelihood reporting requirements for MCC's independent engineers (page 6).

Detailed findings appear in the following section. Appendix I presents the audit scope and methodology. Appendix II presents MCC's comments. MCC disagreed with Recommendation 1 and agreed with Recommendations 2 and 3. Management decisions have been reached on Recommendations 2 and 3, but MCC will need to provide additional documentation before final actions can be taken.

AUDIT FINDINGS

MCC Did Not Conduct Adequate Due Diligence

MCC required a thorough evaluation of the proposed Tanzanian projects before the compact was signed. The Proposal Assessment and Compact Development guidance states, "For each component, due diligence will address technical, economic and environmental feasibility as well as implementation issues and sustainability."

However, when the Tanzania compact was signed in February 2008, MCC lacked critical information surrounding several major projects. For example, the compact included a $53 million hydropower plant construction project, but MCC was unaware of extensive environmental risks at the proposed site. Although a scientific expert published a study in 2005 identifying three new species (Igamba Suckermouth Catfish, Igamba Goby Cichlid, and Igamba Golden Snail) and calling for additional research at the site,[1] MCC was not aware of this report until after signing the compact. MCC conducted additional research in 2009 and concluded that the project would likely destroy or critically alter the entire habitat of the three newly identified species at the project site, so MCC canceled the project.

Similarly, the compact included $35 million for the design and construction of water sector activities, which were subsequently rescoped to eliminate the construction component but retain the design component. According to MCC officials, this activity was among the least defined within the compact at the time of signing. Additional information indicated that the economic rate of return for this activity would be very low and the estimated costs were over budget, so MCC canceled the construction.

In another example, MCC's initial cost estimates for the roads projects proved significantly low, requiring subsequent revisions that led to budget shortages. Officials stated that the estimates were based on the best information MCC had at the time and that construction costs rose following development of the estimates. Finally, MCC significantly underestimated the resettlement costs associated with several projects. For example, the Distribution Systems Rehabilitation and Extension Activity resettlement costs were understated by at least $6 million because MCC did not realize that more than 10,000 people would be affected.

MCC lacked critical information at compact signing because officials did not gather and analyze sufficient information during due diligence. MCC's compact development guidance does not specify which studies will be required during due diligence. MCC officials stated that the feasibility studies they rely upon are sometimes insufficient. Officials also noted that in some cases, MCC is under political pressure to sign compacts quickly, and as a result, work can be rushed, leading to problems during implementation.

Because of inadequate due diligence, MCC was forced to make substantial changes to the compact projects during implementation, with some negative consequences.

[1] Ellinor Michel et al., *Malagarasi Aquatic Ecosystems: Biodiversity & limnological functioning of the Malagarasi-Moyovosi wetlands, western Tanzania* (2005).

Cancellation of the hydropower plant disappointed residents of the region, who have very limited electrical service. While cancellation may have been appropriate, this disappointment could have been avoided if MCC had canceled the project during due diligence. Another consequence is a projected budget shortfall of $134 million, which the Government of Tanzania is expected to pay. Therefore, we are recommending the following:

> ***Recommendation 1.*** *We recommend that the Millennium Challenge Corporation amend its compact development policy to identify the requisite studies that will be completed prior to compact signing.*

Tanzanian Government Funding for Shortfall Not Guaranteed

All projects must be completed by September 2013, when the compact ends. The compact states that it shall remain in force for five years, and that all disbursements, other than those related to compact closure, shall cease upon expiration of the compact in September 2013.

MCC officials anticipate a shortfall of up to $134 million, primarily in the transport sector, which they attribute to rising construction costs. MCC plans to rely upon the Government of Tanzania to finance the shortfall. The Tanzanian government has submitted a letter to MCC showing its willingness to pay up to $134 million, beginning in July 2011. MCC has stipulated that the Tanzanian government meet several milestones within its own budget preparation process in order to receive MCC's approval for disbursements to MCA-T. There is a risk, however, that the Tanzanian government may not provide the funds in a timely manner. Contractors, other donors, and officials from various Tanzanian government agencies told the OIG that the Government of Tanzanian may have overcommitted itself. Further, the officials stated that even if the Tanzanian government had the money, it may not provide the funds in a timely manner. To illustrate, on one recent non-MCC road project financed by the Government of Tanzania, the Government delayed payment to the contractor, causing work to stop for several months.

When faced with the budget shortfall, MCC and the Government of Tanzania initially chose not to rescope in Tanzania, as MCC has in other countries. An MCC official explained that rescoping was not an option at the time because the Government agreed that it would pay for the cost overruns. MCC felt that the best approach was to move forward with the projects as intended and use the Government funding to bridge the gaps in the later years of the compact.

However, without full and timely funding, work on the projects would stop, causing delays and potentially jeopardizing completion within the compact's timeframe. MCC officials said they may have to reconsider rescoping if the funding is not provided. Therefore, we are recommending the following:

> ***Recommendation 2.*** *We recommend that the Millennium Challenge Corporation monitor the Government of Tanzania's progress toward meeting the milestones that the Millennium Challenge Corporation has outlined for funding the budget shortfall, document decisions made during this process, and report to the Office of Inspector General regarding the Government's efforts.*

MCC's Approach Toward Ensuring Worker Safety and Livelihood Needs Improvement

MCC's authorizing legislation, the Millennium Challenge Act of 2003, Section 605(e) (point 3), prohibits MCC from providing assistance to any project "likely to cause a significant environmental, health, or safety hazard." As part of its efforts to manage health and safety risks, MCC requires contractors to develop, implement, and comply with a site-specific Health and Safety Management Plan. MCC also requires contractors to comply with local labor laws.

MCC's approach to ensuring worker safety in Tanzania was not always effective. OIG visited one MCC-funded road construction site in October 2010 and found that the contractor was not fully complying with the Health and Safety Management Plan. That is, the contractor did not provide proper induction safety training, adequate equipment, or water to workers on the site, although these were all required in the contractor's Health and Safety Management Plan. MCA-T and MCC were not aware of some of the safety violations. Monthly reports from the contractor and supervisory firm for MCA-T and from the independent engineer for MCC focused primarily on the road's construction and did not accurately reflect safety conditions in the field. The reports did not properly report all health and safety violations that occurred on the site. Furthermore, the supervisory firm's monthly reports incorrectly stated that adequate equipment and water had been provided to the workers.

All new employees were to receive induction safety training to prepare them for their jobs. The training was to address topics such as personal protective equipment, heat stress, defensive driving, safe operation of heavy equipment, first aid, use of fire extinguishers, reporting of accidents, and use of different equipment. The contractor said that it did not provide induction safety training.

Similarly, the contractor did not provide appropriate personal protective equipment to some workers. During the site visit, the audit team observed that shoes provided by the contractor to a worker were canvas athletic shoes rather than the safety boots required in the Health and Safety Management Plan. According to contractor officials, they provided some workers with sport shoes instead of work boots because not all of the boots had arrived on site yet.

Finally, the contractor confirmed that it did not provide drinking water to the workers, although the plan requires this and recognizes that working in the heat could result in a wide range of problems, from minor health concerns to death. In addition to the safety violations, some workers were working overtime, but were not always compensated for the additional hours. Although Tanzanian labor laws outline the circumstances for paying overtime wages, the contractor did not always comply with the laws.

The audit team also found that the Health and Safety Management Plans prepared by two different road construction contractors varied significantly in specificity and practicality. For example, one plan included contact information for the project and health and safety managers, onsite clinic information, and medical evacuation information, if a worker is injured on site. The second plan indicated that injured workers would be given medical treatment onsite and transported to a hospital if necessary, but details such as where the injured workers would go were not specified. Furthermore, although MCC knew that the second plan lacked detail and contained generic information, an MCC official told MCA-T not to hold it up because MCC did not want to delay work on the road.

As part of a separate audit,[2] the OIG team returned to this road construction site in February 2011 and was told by MCC and MCA-T officials that the contractor had provided additional protective gear, including sturdy boots, and water to the workers and that workers were now receiving proper wages. Despite the improvements at this site, MCC's approach could be further strengthened.

MCC's oversight mechanisms did not identify some of the safety violations we observed because MCC's practices and procedures do not adequately monitor compliance with or violations of the plans. MCC relies on various parties to conduct oversight in the field, but does not have specific reporting requirements for any health and safety violations, including serious accidents or deaths. MCC officials said that adopting international best practices would strengthen their current approach toward ensuring worker safety.

Noncompliance with Health and Safety Management Plans increases the risk of worker injury, additional project costs, delays, and poor quality of work. Ultimately, an unsafe work environment will interfere with MCC's ability to complete the projects and damage MCC's reputation. To address these deficiencies, we are recommending the following:

> ***Recommendation 3.*** *We recommend that the Millennium Challenge Corporation strengthen its occupational health and safety policy by (a) adopting international best practices, (b) providing guidance to Millennium Challenge Accounts on implementing the policy, (c) developing standards for contractors' Health and Safety Management Plans, and (d) establishing worker safety and livelihood reporting requirements for the Millennium Challenge Corporation's independent engineers.*

[2] OIG Review of Government-Owned Enterprises.

OTHER MATTERS FOR CONSIDERATION

Project Delays Could Occur if MCC's Mitigation Efforts Fail

All projects must be completed by September 2013, when the compact ends. However, the transport and energy projects face considerable risks that could delay their completion if MCC's mitigation efforts fail. MCC recognizes the significance of these risks and has developed mitigation efforts to address them.

In the transport sector, contractors have encountered unexpected delays in the tax exemption process when receiving shipments from the port. These delays limit contractor access to equipment and may contribute to project delays. Periodic backlogs develop within the Tanzanian Government agency responsible for granting the exemptions. MCA-T has attempted to improve the situation by providing contractors a checklist to help ensure that their paperwork is filed correctly as they move through the process and by encouraging the Tanzanian Government officials involved to expedite the process.

Also within the transport sector, managing the Mainland Roads activity has been challenging. The Tanzanian Government entity responsible for overseeing this activity has limited project management capacity. In addition, because of limited training and experience, MCA-T has been unable to use the management tool provided by MCC (Microsoft Project) to manage the project efficiently. As a result, MCC supported MCA-T's decision to hire a project management consultant to help manage the Mainland Roads activity.

In the energy sector, resettlement associated with the Distribution Systems Rehabilitation and Extension Activity has proven much more extensive than MCC anticipated, affecting more than 10,000 persons. Each person must be compensated, and the affected site must be cleared before construction can proceed. As the magnitude of the effort became apparent, MCC supported MCA-T's efforts to expand the resettlement contractor's focus, the project's timeframes were extended, and the budget was increased by more than $6 million to accommodate the resettlement.

MCC has recognized the significance of these risks and has taken steps to mitigate them. However, if MCC's mitigation efforts fail, the resulting delays could threaten the projects' completion within the compact's timeframe. Because MCC has taken actions to mitigate these risks, OIG is not making recommendations at this time.

EVALUATION OF MANAGEMENT COMMENTS

The Millennium Challenge Corporation (MCC) provided written comments on the draft report that are included in their entirety in appendix II of this report. We reviewed the comments and revised the report as appropriate, to address the comments. In its comments, MCC disagreed with one recommendation and agreed with two recommendations.

MCC disagreed with Recommendation 1, to identify the requisite studies that will be completed prior to compact signing. MCC said that it is not possible to create a specific checklist or single list of requisite studies to be completed prior to compact signing because each potential compact project varies greatly from country to country, by sector, and by the unique mix of activities or interventions proposed. MCC also disagreed that the instances cited in the report, other than the Malagarasi Hydropower activity, are indicative of inadequate due diligence.

OIG's position is that the identification of requisite studies to be completed prior to compact signing would strengthen MCC's due diligence process and help reduce problems during implementation. OIG considers that a management decision has not been reached on this recommendation.

MCC agreed with Recommendation 2, to monitor the Government of Tanzania's progress toward meeting the milestones MCC has outlined for funding the budget shortfall, document decisions made during this process, and report to OIG regarding the Government's efforts. MCC is confident that the Government of Tanzania will fund the shortfall, and MCC is monitoring the Government's progress toward doing so. OIG considers that a management decision has been reached. However, final action will not take place until MCC provides OIG with documentation that the funding has been obtained.

MCC agreed with Recommendation 3, to strengthen its occupational health and safety policy by (a) adopting international best practices, (b) providing guidance to Millennium Challenge Accounts on implementing the policy, (c) developing standards for contractors' Health and Safety Management Plans, and (d) establishing worker safety and livelihood reporting requirements for MCC's independent engineers. MCC explained that the International Finance Corporation's Social and Environmental Safeguards will be incorporated as official MCC policy in 2011. MCC said the revised policy will provide accountable entities with more consistent and clear guidance and standards for addressing key health and safety issues with their contractors and others involved in compact development and implementation. MCC will also require that accountable entities establish a comprehensive social and environmental assessment and management system that includes reporting mechanisms for data on occupational health and safety, among other things. OIG considers that a management decision has been reached. However, final action will not take place until MCC provides OIG with the updated MCC policy and associated requirements for accountable entities.

SCOPE AND METHODOLOGY

Scope

The Office of Inspector General conducted this audit of the Millennium Challenge Corporation's (MCC's) funding of activities in Tanzania in accordance with generally accepted government auditing standards. These standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides that reasonable basis.

We conducted an audit of MCC's funding of activities in Tanzania because the compact is one of MCC's largest and it is nearly at the midpoint of implementation. We conducted our fieldwork from August 17 to December 9, 2010, at MCC headquarters in Washington, DC, with a site visit to the Millennium Challenge Account-Tanzania (MCA-T) in Dar es Salaam from September 27 to October 15, 2010. In Tanzania, we conducted site visits to an energy project on Zanzibar Island and a road project in the town of Tanga.

We interviewed officials at MCC's headquarters and MCA-T, contractors, implementing entities, and other donors to draw their conclusions about the Tanzania compact. We obtained and analyzed MCC documentation supporting the due diligence process and the conclusions MCC reached during it. We analyzed various aspects of the project to determine whether MCC had identified and mitigated the major risks. During the site visits, in addition to interviewing project officials, we interviewed residents affected by the projects to further our understanding of MCC's resettlement process.

We examined the internal control environment by identifying and assessing the relevant controls, including supporting documentation for the due diligence process and supervisory controls on the road construction project. For example, we assessed a road construction contractor's compliance with the Health and Safety Management Plan, and reviewed reports from the supervisory and independent engineers. The contract for the road project was $53.9 million and the contract for the energy project was $29.5 million, both of which represent approximately 14 percent of the costs in their sectors.

Methodology

To answer the audit objective, we established audit steps to determine whether MCC and MCA-T identified and mitigated the major risks facing the compact program in Tanzania. Specifically, we performed the following activities:

- Interviewed MCC and MCA-T officials to gain an understanding of the project activities and associated risks and mitigation efforts
- Interviewed contractors, implementing entity officials, and other donors to gain their perspectives on the risks facing the projects
- Reviewed documents supporting the project activities, including the compact, due diligence documents, the monitoring and evaluation plan, detailed financial plans, resettlement action plans, Health and Safety Management Plans, and contracts

- Judgmentally selected two projects for our site visits, in part because they were furthest into implementation
- Met with individuals involved with resettlement to understand that process

MANAGEMENT COMMENTS

MILLENNIUM
CHALLENGE CORPORATION
UNITED STATES OF AMERICA

DATE: March 11, 2011

TO: Mr. Alvin Brown, Assistant Inspector General
Millennium Challenge Corporation

FROM: Mr. Patrick Fine - Department of Compact Operations
Millennium Challenge Corporation

Dear Mr. Brown:

The Millennium Challenge Corporation (MCC) appreciates the opportunity to respond to the Office of Inspector General's (OIG) draft report entitled "Audit of the Millennium Challenge Corporation's Funding of Activities in Tanzania."

MCC's specific responses to the three recommendations in the draft report are detailed below and in the supplemental information provided as part of this letter which contains information and corrections to specific statements presented in the audit report.

Recommendation 1: We recommend that the Millennium Challenge Corporation amend its compact development policy to identify the requisite studies that will be completed prior to compact signing.

MCC Response: MCC does not agree with the recommendation.

MCC's current due diligence standards require that MCC address, to the maximum extent possible, the technical, economic, environmental, and social feasibility of each component of a compact, including foreseeable implementation and sustainability issues. It is not possible to create a specific checklist or single list of requisite studies to be completed before each compact, because each potential compact project or component varies greatly from country to country, by sector, and by the unique particular mix of proposed activities or interventions proposed. MCC notes that current due diligence standards and guidance are comparable to standards applicable to USAID.

MCC agrees that its due diligence efforts for the Malagarasi Hydropower Activity could have been more robust. However, MCC does not agree that the recommended amendment is required as a result. MCC also does not agree that the instances cited (other than that relating to Malagarasi Hydropower Activity) are indicative of inadequate due diligence or lack of a defined set of requisite studies. On the contrary, they represent examples of

MCC's willingness to be flexible when implementing long-term international development programs (of up to 5 years) with a fixed budget, where actual costs vary and host country needs and priorities change or are redefined. The increasing cost of road construction throughout Tanzania over time is a good example. Cost estimates for the road projects in the Tanzania Compact were made in 2007, based on the best available market information at the time. These estimates turned out to be too low. In fact, actual costs for infrastructure projects financed by *all* donors and Government of Tanzania (GoT) have increased significantly in the past several years for a variety of factors that no one could have accurately predicted, and not due to "lack of critical information," or "inadequate due diligence" by MCC, other donors or GoT. MCC-financed contracts remain fully in line with current market prices based on the best and most up-to-date data from all donors.

The Non-Revenue Water (NRW) Reduction Activity is an example of MCC's effort to adjust quickly to changing conditions while taking part in the greater donor community efforts. At the time of Compact negotiations, another project to develop a deep water aquifer system was found not feasible on technical grounds thus elevating the NRW Activity into the Compact. The rapidly changing conditions of the Dar es Salaam water distribution network made the development of this activity more logical post Compact signing. In this development phase, two large construction projects were promoted by the GoT Water Sector Development Program as an effective means to meet the Activity's objectives. However, the plans and information presented required further evaluation. After updating the plans and re-evaluating the project's costs, it was determined that current market conditions made the project no longer feasible. As a result of this finding those remaining funds have been re-invested into other NRW priorities and Water Sector Project activities to meet the Compact's objectives.

MCC's decision to significantly modify the Malagarasi Hydropower Activity after all available environmental factors became known was, and remains the correct decision for all concerned. Although MCC carried out high-level environmental screening and due diligence on the proposed hydroscheme during Compact development, a full and final environmental analysis could not be completed until project feasibility and design studies were underway during the second year of the Compact. It was this final environmental analysis which revealed that the project would certainly create a significant environmental hazard, even with the inclusion of mitigation measures. Thus, pursuant to section 605(e)(3) of the Millennium Challenge Act of 2003, which prohibits MCC from funding projects "likely to cause a significant environmental…hazard", MCC elected to descope the Malagarasi Hydropower Activity. Since the modification of the Activity, a new location for a larger, more powerful and environmentally benign hydroscheme has been selected and feasibility and design work is well underway. In addition, some of the Activity funds are now supporting the design and implementation of a sustainable solar energy program for the town of Kigoma. The original driver for the Activity was the need for additional, more reliable and affordable sources of power for Kigoma, both in the short and long term. Both of the efforts currently receiving Compact funding through the current version of the Malagarasi Activity are supporting these goals and doing so in an environmentally sustainable manner.

Recommendation 2: We recommend that the Millennium Challenge Corporation monitor the Government of Tanzania's progress toward meeting the milestones that the Millennium Challenge Corporation has outlined for funding the budget shortfall,

document decisions made during this process, and report to the Office of Inspector General regarding the Government's efforts.

MCC Response: MCC agrees with the recommendation.

MCC did not set these milestones lightly; they were set up after MCC thoughtfully considered the GoT proposal to cover the shortfall; confirmation from the International Monetary Fund that GoT had the fiscal space to meet such a commitment. Furthermore, the Tanzanian President and Minister of Finance made explicit assurances that GoT was fully committed to cover any cost overruns through its annual budget appropriations process. MCC monitors the milestones set forth in the letters exchanged between the GoT and MCC regarding the budget shortfall. Through such monitoring, MCC will have firm evidence as to whether the GoT is meeting its budgetary commitments before any funds are needed and will be able to make timely re-scoping adjustments, if any, in partnership with the GOT.

Recommendation 3: We recommend that the Millennium Challenge Corporation strengthen its occupational health and safety policy by: (a) adopting international best practices, (b) providing guidance to Millennium Challenge Accounts on implementing the policy, (c) developing standards for contractors' Health and Safety Management Plans, and (d) establishing worker safety and livelihood reporting requirements for the Millennium Challenge Corporation's independent engineers.

MCC Response: MCC agrees with the recommendation.

Independent of this audit, MCC has been working over the last several months towards strengthening its policy and approach for handling occupation health and safety issues. A key component of this effort is MCC's decision to incorporate the International Finance Corporation's (IFC) Social and Environmental Safeguards (the "Performance Standards") as official MCC policy. The IFC's Performance Standards are considered international best practice and specifically address occupational health and safety issues, among other key environmental and social issues. MCC plans on adopting an updated version of the Performance Standards that IFC expects to issue in the Spring of 2011. Once these Performance Standards are incorporated into MCC policy, accountable entities will have more consistent and clear guidance and standards for addressing key health and safety issues with their contractors, government counterparts, local leaders, and others involved in compact development and implementation. In addition, upon adopting the Performance Standards, MCC will require that accountable entities establish a comprehensive social and environmental assessment and management system that includes effective and timely reporting mechanisms that will cover, among other issues, data on occupational health and safety.

Current MCC policy requires that under all contracts between MCA-Tanzania (or any other accountable entity in any country) and the contractors, the contractors must comply with all applicable laws of the country, including overtime and other labor laws, as well as laws relating to health, safety, workers' compensation, and taxes, among others. Supervisory Engineering firms are also contractually required to manage the contractors and ensure that these provisions are enforced. In the case of the road project audited in Tanzania, MCC and

MCA-Tanzania were aware that both the contractor's and the Supervisory Engineer's performance of this requirement was inadequate. Therefore, MCC has supported, and will continue to support, MCA-Tanzania's efforts to ensure better compliance in the future, using the existing contractual mechanisms to improve performance. In addition, official reporting requirements are standard in FIDIC contracts, are included in the Health and Safety Management Plans and cover contractor reporting requirements to the Supervisory Engineer and MCA-Tanzania. Lastly, MCC's official guidance on establishing Health and Safety Management Plans is included in our Environmental Guidelines and Standard Bidding Documents.

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In addition to the responses in the management response letter, MCC has found the following factual inaccuracies within the draft report which are addressed herein.

On page four, the draft audit report states, "All projects must be completed by September 2013, when the compact ends…. MCC may not meet this deadline, however, because a projected budget shortfall could cause work to stop unless rescoped." This statement is inaccurate. The risk of any potential budget shortfalls is not correlated with risk of delay; they are separate and independent risks. If there is a budget shortfall, a rescoping decision would require that all proposed activities must be completed within the timeframe of the Compact.

On page four, the draft audit report states, "An MCC official explained that rescoping was not an option because the Government agreed that it would pay for the cost overruns." This statement is inaccurate. MCC considered rescoping as an option (alongside several other options) and elected not to rescope.

On page four, the draft audit report states, "Contractors, other donors, and officials from various Government agencies told the OIG that the Government of Tanzania may have overcommitted itself." Hearsay comments from officials not directly responsible for this matter do not provide a basis for policy. The fact is that the authorized, responsible Government officials have legally committed the government. MCC did consult with the IMF who advised (in writing) that this is within the GOT's fiscal capacity. In light of our response to Recommendation 2, we find this assertion irrelevant. Moreover, it is unclear how reporting hearsay comments without attribution is intended to improve MCCs performance on this point.

On page five, the draft audit report states, "the contractor did not provide proper induction safety training, adequate equipment, or water to workers on the site, although these were all required in the contractor's Health and Safety Management Plan." This statement is inaccurate and overly broad. Generally, the contractor was compliant, however, there are instances when the contractor did not consistently provide all of these things at all the times required or to all workers.

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